Office - Supreme Court
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IN THE

SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1952.

No. 467

IN THE MATTER OF V-I-D, INC.,
Debtor,

KELLEY, GLOVER & VALE, Incorporated, Trustee,
Petitioner,

vs.

CHARLES J. KRAMER and HELEN KRAMER, and PETER EVANS, Successor Indenture Trustee,
Respondents.

PETITION FOR WRIT OF CERTIORARI, to the United States Court of Appeals, For the Seventh Circuit

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(1)

The decision below resurrects respondents' first mortgage lien which had become *permanently unenforcible* in the Indiana State Courts, and enforces it against Indiana real estate, which results in destroying petitioner's admittedly valid and matured second mortgage. This violates basic principles, regardless of whether the *Erie R. R.* v. *Tompkins* doctrine should be applied 9

(2)

It perverts the bankruptcy court's administrative function of distributing assets to creditors, into the arbitrary power of *reversing* the matured and vested lien rights of these two mortgage holders, as compared to what the state courts would do, and with no overriding federal law to justify it. This directly violates the principles of both opinions in *Vanston Bondholders' Protective Committee* v. *Green,* 329 U. S. 156, on which the decision below purports to be based. (Tr. 126) 10

(3)

While petitioner's rights do not depend on *Erie R.* v. *Tompkins,* the decision below sets an erroneous precedent by *excluding* that doctrine *generally* from the bankruptcy courts on non-federal questions such as the validity of these *matured* lien rights on real estate 13

(4)

By expressly holding that bankruptcy courts are not bound by state statutes making contracts of non-complying foreign corporations unenforcible (Tr. 126), the decision emasculates this regulatory police power of the states, and turns the bankruptcy courts into a sanctuary for such corporations to reap the fruits of their unauthorized business, in defiance of the states and their courts 16

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THE MATTER INVOLVED.

The sole contestants here are the holders of a contested first mortgage "trust indenture" on Indiana real estate (respondents) and the holder of an admitted second mortgage on the same real estate (petitioner).

The contest consists of the second mortgage holder's assault upon the first mortgage as being invalid and unenforcible under Indiana law, because it arose out of unauthorized transaction of business in Indiana by a non-complying foreign corporation.

Each mortgage is larger than the value of the real estate, so the contest is, which one will get it. (Tr. 124). Normally, this contest would have been in an Indiana state court where the real estate lies (Tr. 95) and where the petitioner and two of the respondents (the Kramers) reside.

This contest was thrown into the forum of the bankruptcy court by the fortuitous or designed circumstance that in 1939, long after both mortgages had *matured,* the debtor corporation,V-I-D, Inc., took a quit-claim deed to this real estate *subject* to the mortgages but without assuming to pay either of them. (Tr. 95-96). Four months and one day after taking title, it filed this reorganization proceeding which is still pending. (Tr. 96). Neither mortgage is a *debt* of the debtor corporation, but the bankruptcy court became the forum for this contest because its Trustee is holding possession of the real estate (the question of whether the bankruptcy court should have abandoned the real estate for litigation in the state court not having been raised below). Further factual details, not directly bearing on this petition, are stated in the footnote.[1]

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[1] Home Bank and Trust Company of Chicago, Illinois, charted as an Illinois banking corporation (Tr. 74) but never licensed or authorized to transact business in Indiana (Tr. 51), nevertheless created 50 to 100 first mortgage bond issues on Lake County, Indiana, real estate in the late 1920's as part of its investment banking business (Tr. 49), "just the way they (bank and officers) would handle Chicago (Illinois) property." (Tr. 51).

One of these transactions was the bank's loan of $135,000 to Charles Baran and wife, residents of Lake County, Indiana, secured by this first mortgage (trust indenture) upon this real estate then owned by the Barans in that county, on December 30, 1927, due December 30, 1934. (Tr. 51, 78, 80). The mortgage and bonds secured thereby were executed by the Barans in Gary, Lake County, Indiana. (Tr. 57, 85-86). The bankruptcy court found this constituted unauthorized doing of business in Indiana by this banking corporation. (Tr. 97-98).

The bankruptcy court ordered its Trustee not to participate in this contest of these mortgage holders but to abandon the field to them, because there is no equity for the debtor corporation or its estate in any event, but simply a contest as to which mortgage holder gets the real estate. (Tr. 124).

This first mortgage (trust indenture) runs to this bank and Lawrence H. Prybylski as co-mortgagees-trustees. (Tr. 78). Prybylski was the bank's vice-president. (Tr. 48). That was "the only reason he was named" as co-mortgagee-trustee. (Tr. 56, top). It appears from a recital on the face of this first mortgage that the bank, apparently being aware of the unauthorized nature of its transaction, used this vice-president in this manner in an attempt to bolster the transaction "whether or not the same shall lawfully run in favor of or be conferred upon or be enforcible by the Home Bank and Trust Company and its successors in trust hereunder" (Tr. 85). Prybylski died in 1950 (Tr. 13).

Also named in the mortgage as the bank's successor "with identical powers and authority" was respondent Evans (Tr. 85) who was the bank's president (Tr. 47). He asked to be and was ordered substituted as successor mortgagee-trustee under the first mortgage claim in this proceeding "instead of Home Bank and Trust Company and Prybylski" in the words of Mr. Lyddick, counsel for respondents Evans and Kramer. (Tr. 40). This substitution was made on November 1, 1950 during the hearing of the objections to the first mortgage claim (Tr. 93).

Respondents Kramer, husband and wife, are holders of $101,000 principal amount of the $135,000 first mortgage bond issue. (Tr. 124). They acquired all of them after the 1934 maturity date, beginning in 1936, many of their bonds being obtained by bartering merchandize at from 15c to 35c on the dollar. (Tr. 98).

Petitioner, Kelley, Glover & Vale, Incorporated, Trustee, is the original and present holder of a second mortgage executed by the Barans' grantees, Gerometta and wife, on the same real estate on June 20, 1928, six months after the first mortgage. (Tr. 7). This mortgage went to foreclosure decree in a state court on February 5, 1931 in the principal sum of $38,970.88 with interest from that date at 6% per annum (Tr. 124). The real estate never was sold under this decree, so the effect of the decree was to fix the amount of the second mortgage lien and keep it alive for future execution against the real estate by the state court. (Tr. 7-9). This second mortgage and decree thereon was filed as a claim against this real estate but not as a debt of the debtor corporation on August 19, 1950. (Tr. 6-10).

No question of distribution of assets between the debtor's creditors is involved, since neither contestant is a *creditor* of the debtor, but both are *lienholders* on this real estate. The issue between the two lienholders is not the proper *sharing* of assets between them but *a winner-take-all contest* depending on the *validity* of the first mortgage. (Tr. 94, 124).

Issues were joined by these contestants in the bankruptcy court by means of a so-called "claim" filed by the first mortgage holders (respondents), *not* asserting a *debt* of the debtor corporation but asserting the *validity* of the first mortgage and bonds secured thereby as a *first lien* on the real estate (Tr. 2-6, 94), and objections filed against that "claim" by the second mortgage holder (petitioner) asserting the *invalidity* of the first mortgage. (Tr. 94). So far as pertinent here, the objections were grounded upon one issue of fact and one issue of law, namely:

> **In fact,** the objector asserted: The first mortgage arose out of unauthorized business in Indiana by a non-complying (non-licensed) foreign corporation mortgagee, Home Bank and Trust Company, of Chicago, Illinois, whose successors in interest are the respondents. (Tr. 97, 98).
>
> **In law,** the objector asserted: An Indiana statute closed the doors of the state courts against enforcement of this unauthorized mortgage. (Tr. 125). This *bar* is *permanent* and *incurable* because the foreign corporate mortgagee never did comply and *never can* comply because it has ceased to exist as a corporation. (Tr. 48, 97). The bankruptcy court must follow the Indiana statute in *this* situation, particularly since the case does not involve competing *claims* against the *debtor* corporation but competing *liens* against

this *real estate.* The bankruptcy court is powerless to validate and in effect *create* a lien which *never was* and *never can be* enforcible in the state courts. (Tr. 98-99).

The decision: The bankruptcy court found the above fact issue in favor of the objector-petitioner,—that the first mortgage arose out of unauthorized transaction of business in Indiana by the non-complying foreign corporate mortgagee, that this mortgagee "was *never* licensed to do business in Indiana * * * and that it *ceased to exist* as a banking institution about 1935" (Tr. 97), four years prior to the reorganization proceeding in 1939, and therefore *never can* become licensed in Indiana to cure the non-compliance.

But the bankruptcy court decided the law issue in favor of the first mortgage, holding "there seems to be *no reason* why this *statute* would close the door of the *federal courts* to *such a corporation,* * * *" (Tr. 99), adjudging that the first mortgage is valid, and overruling the objections. (Tr. 104).

The Court of Appeals accepted the above fact finding of the bankruptcy court (Tr. 124) and also affirmed the bankruptcy court's legal doctrine by the following passage in its opinion, which is the crux of the question presented by this petition:

> "However, we *need not dwell* on the question of whether the present owners of these bonds *could* maintain in an action on the bonds in the *Indiana* state court *because* their claims were presented in a *bankruptcy court.* The Supreme Court has repeatedly held that in the allowance of claims a bankruptcy court is *not required to follow state statutes.*" (Our italics). (Tr. 126)

The opinion predicated the above ruling principally upon **Vanston Bondholders Protective Committee v. Green et al, 329 U. S. 156, 162.** (Tr. 126). The opinion held inapplicable **Woods v. Interstate Realty Co., 337 U. S. 535,** and **Erie R. R. v. Tompkins, 304 U. S. 64,** on the theory that the doctrine of the *Tompkins* case is *restricted* to diversity of citizenship cases, and that the federal courts are free to disregard state statutes in bankruptcy cases. (Tr. 127-128).

Petitioner's version of what is the Indiana law stands admitted for the purpose of this petition, because both the bankruptcy court and the Court of Appeals adopted the *premise* that the Indiana courts were *closed* against the enforcement of the first mortgage but decided that *nevertheless* the bankruptcy court was *open* to its enforcement "because" that court "is not required to follow state statutes." (Tr. 98-99, 126).

Likewise admitted for present purposes, is petitioner's contention that the non-complying mortgagee's successors (respondent Evans as successor trustee-mortgagee and respondents Kramer as bondholders) stand in its shoes and in no better position. The Court of Appeals based these respondents' right to recover, not upon any new or superior rights, but upon the *premise* that the first *mortgage* is enforcible in the bankruptcy court *notwithstanding* the Indiana statute. (Tr. 126).

However, if the unenforcibility of this first mortgage in Indiana courts needs to be demonstrated here, Indiana's construction of her statute squarely upholds petitioner's contention in two cases later than those cited in the opinions below. (Tr. 99, 125). **Barnett v. Central Republic Bank and Trust Co. (1935) 100 Ind. App. 495, 496, 500, 196 N.E. 369, 371. Burroughs v. Southern Colonization**

Co. (1932) 96 Ind. App. 93, 103-104, 106, 173 N. E. 716, 719, (transfer denied by Indiana Supreme Court). These cases are in point with this situation, whereas those cited in the opinions below are not, as shown in the next paragraph.

A confusing and immaterial point of Indiana law which does not form the basis of the Court of Appeals' opinion but is stated therein in confusing and ambiguous fashion,— that a non-complying corporation's contract is not void, but unenforcible in Indiana courts, and *becomes* enforcible *if* the corporation complies (becomes licensed) after making the contract (Tr. 125),— is conceded by us. But this foreign corporation, Home Bank and Trust Company, **went out of existence** in 1935, never did comply, and **never can comply,** as testified by respondent Evans (Tr. 48) and found by the bankruptcy court. (Tr. 97). Under this admitted state of facts (unmentioned and ignored in the Court of Appeals' opinion) the Indiana law is well settled that this is a good **defense in bar** against foreclosure of a mortgage taken by the non-complying corporation, **Barnett v. Central Republic Bank and Trust Co. (1935) 100 Ind. App. 495 at p. 500, 196 N.E. 369, 371,** even though in that case, as here, a successor mortgagee-trustee, was named in the mortgage and became substituted in the foreclosure proceeding. (100 Ind. App. at p. 496).

Also eliminated from this petition is a superficially similar but different Indiana statute forbidding non-residents, *individual* or corporate, to become trustees of Indiana real estate. That statute (Sec. 56-620 Burns Ind. Sts.), which forms part of the chapter on real estate trusts and powers, was relied on by us below as an independent point of objection against the first mortgage, and was ruled against us as an independent point in the bankruptcy

court's opinion (Tr. 98) and in the Court of Appeals' opinion (Tr. 128). The latter opinion correctly says that our "principal contention" is based upon the totally distinct foreign corporation statute of Indiana, (Tr. 124-125), which is the only statute involved in this petition.

The decisions below are reported as:

In re: *V-I-D, Inc.* (D.C. N.D. Ind.) 101 F. Supp. 71

In re: *V-I-D, Inc.* (7 Cir), 198 F. 2d 392

The headnotes and editorial summaries of both opinions in the above publications are inaccurate and inadequate on the point presented in this petition. The point here involved (whether the bankruptcy court is bound to follow the Indiana statute in this situation) appears in the bankruptcy court's opinion, 101 F. Supp. at page 74, point 3, (Tr. 98-99), and in the Court of Appeals' opinion, 198 F. 2d at page 395, first column. (Tr. 126).

Basis of this Court's Jurisdiction.

Jurisdiction here is based on 28 U.S.C. 1254(1). A timely filed petition for rehearing (Tr. 137) was entertained and denied on August 28, 1952 (Tr. 145) and this petition is filed within ninety days thereafter.

QUESTIONS PRESENTED.

The sole question is whether a bankruptcy court sitting in Indiana is required to give effect to an Indiana statute closing the doors of the Indiana courts against enforcement of this first mortgage on Indiana real estate:

(a) where the fact situation is such that the first mortgage, larger than the value of the real estate, had become *forever barred* from enforcement in the

Indiana courts, *before* the bankruptcy court's jurisdiction attached;

(b) where a matured second mortgage, also larger than the value of the real estate, had become entitled to take the real estate in the Indiana courts under Indiana law by virtue of the invalidity of the first mortgage, before the bankruptcy court's jurisdiction attached;

(c) where there is no equity in the real estate for the debtor corporation, and *no question of distribution* between *creditors* of the debtor corporation, but only a contest of *lien validity* between these two so-called "claimants" who are not creditors of the debtor corporation but merely holders of mortgages which were upon its real estate before it took a quit-claim deed without assuming the mortgages; and

(d) where the bankruptcy court's refusal to give effect to the Indiana statute has the effect of completely reversing the lien and property rights of the contestants,—giving the entire real estate to the first mortgage holder who could not have touched it in the state courts, and completely freezing out the second mortgage holder who would have taken all in the state courts.

REASON FOR ALLOWANCE OF WRIT.

The need for certiorari will be self-apparent, we think, from the foregoing statement of the matter involved and the questions presented, without much elaboration.

(1)

Regardless of whether the *Erie R. R.* v. *Tompkins* doctrine applies here, the result below violates basic principles

of vested property rights, division of powers between state and federal courts, and the scope of bankruptcy jurisdiction, which have existed from the beginning and which stem from the Constitution. Among these principles are:

(a) Rights to real estate which have become vested and matured cannot be taken away from one citizen and given to another in the absence of some tort or contract obligation betwwen them whereby they create this result for themselves.

What this bankruptcy court did, in effect, was to take this real estate away from the second mortgage holder and give it to the first mortgage holders, by the device of breathing life into a dead first mortgage which was large enough to consume the real estate. This result was not based on any consent or conduct of two mortgage holders —they were strangers at arm's length—but upon a total misconception of the bankruptcy court's *administrative* function of *distributing* a debtor's assets among creditors, and upon a total misapplication of the Supreme Court's decisions on that subject, which we shall presently discuss.

(b) Federal courts are required to follow state statutes as construed by the state courts, particularly relative to vested property rights in real estate located in the state **(28 U.S.C. 1652)**. The same is true of bankruptcy courts relative to matured lien rights. **(8 C.J.S. Bankruptcy, sec. 453)**.

(2)

Under the guise of the bankruptcy court's administrative power to determine claims and distribute assets to creditors, the decision below mistakenly perverts this function and misapplies the Supreme Court's decisions on

that subject. The bankruptcy court here undertook the arbitrary and non-existent power of resurrecting a dead lien and destroying a valid one,—a reversal of vested property rights.

This apparent violation of the due process clause of the **Fifth Amendment** of the Constitution, naturally finds no sanction in the Supreme Court cases which it cites. They go no further than to permit departure from state laws to the extent which is: (1) necessary to carry out the overriding purpose of the Bankruptcy Act and (2) incidental to the function of *distributing* the debtor's assets among *its* creditors. Neither of these justifications exist here,—and in the absence of justification it is judicial usurpation and tryranny.

The case principally relied on in the Court of Appeals' opinion (Tr. 126) is actually directly against it. **Vanston Bondholders' Protective Committee v. Green, 329 U. S. 156.** The opinion overlooks the basic principle in the *Vanston* case that:

> "What claims of creditors are *valid* and subsisting obligations against the bankruptcy at the *time* a petition in bankruptcy is filed is a question which in the absence of *overruling Federal law*, is to be determined by reference to *state law.*" (329 U. S. at p. 161).

There is no "overruling Federal law" which requires, or even permits, the absurd and arbitrary decision which the bankruptcy court rendered here in **reversing the vested property rights of these two lienholders so that the first mortgage which was dead and unenforcible in the state courts now gets the land, and the second mortgage which would have got the land in the state courts now gets nothing.**

Besides finding no support in the majority *Vanston* opinion, the above result *directly violates the following principle in the concurring opinion*:

> "If there was no valid claim *before* bankruptcy, there is no claim for a bankruptcy court either to recognize or to reject. * * * For nothing comes into a bankruptcy court to which congressional policy can apply unless it is an obligation *created* by applicable State law. And no obligation finds its way into a bankruptcy court unless, *by the law of the State* where the acts constituting a transaction *occur*, the *legal consequence* of such a transaction is an *obligation* to pay." (329 U. S. at p. 170). (Our Emphasis).

In three major respects, the fact situation here is the opposite of *Vanston etc.* v. *Green* (1946) 329 U. S. 156, *supra*. The *Vanston* case held the bankruptcy court, in its *distribution* function, could disallow "interest on interest" of a first mortgage where: (1) All this interest matured *during* a federal court receivership and reorganization and the court had forbidden the receiver to pay the interest. (2) This interest was a *debt of* the corporation being reorganized. (3) This power was exercised in aid of *distribution* between the debtor corporation's creditors. This latter point is the one decided in *Prudence Realization Corporation* v. *Geist* (1942) 316 U. S. 89, plus the added feature that the adjustment of equities was between "creditors in the *same class.*" (p. 93). *American Surety Co.* v. *Sampsell* (1946) 327 U. S. 269 involved subrogation of a surety—a point remote from ours—and merely held that bankruptcy law "governs the *distribution* of a bankrupt's assets to *his* creditors" (p. 372),—not that it creates a creditor or creates a lien where none existed before. *Homberg* v. *Armprecht* (1946) 327 U. S. 392 merely held that in a diversity case the federal statute of limitations governs the federally-created liability of shareholders in a joint stock land bank. (p. 395).

The bankruptcy court's administrative power to determine claims and "bring about a ratable *distribution* of assets among the *bankrupt's* creditors" (*Vanston Bondholders Protective Committee* v. *Green*, 329 U. S. 156, 161, *supra*) is no justification for the result below where there was *no equity* in the real estate for the debtor corporation, *no question of distribution* to creditors but a contest of lien validity under an Indiana statute, and where the *only thing done* by the court was to *create* a previously non-existent property right in one party and *destroy* a previously existing property right of another.

This total perversion of the administrative function of the bankruptcy court, and distortion of the Supreme Court precedents cited in the opinion below on the subject of distribution, results from a mixture of confusion and fallacies: (1) Failure to recognize that these mortgages are not *claims* of the debtor corporation's *creditors* but preexisting *matured liens* upon its real estate. (2) Failure to recognize that this is not a question of *distribution* between creditors but a question of adjudging the *existence* or non-existence of an *entire* first mortgage, which depends on Indiana law. (3) Failure to recognize that this bankruptcy court is distorting its administrative power of distribution between creditors to cover an *entirely different field.*

(3)

While the result below violates basic principles antedating **Erie R. R. v. Tompkins (1938) 304 U. S. 64,** as above shown under (1), petitioner would be entitled to invoke that doctrine if necessary, because **the openly express disregard and defiance of its substantive rights under Indiana law in the Court of Appeals' opinion (Tr. 126),** and the result accomplished, violate both the letter and spirit of the *Tompkins* case.

And what is more important; the Court of Appeals' opinion **sets an erroneous precedent expressly excluding the Tompkins case from application in bankruptcy cases generally on the theory that the Tompkins doctrine does not apply in bankruptcy courts,** even though substantive rights of litigants under state law are involved in those courts. (Tr. 126). **The opinion also restricts the Tompkins doctrine to diversity of citizenship cases.** (Tr. 128).

We know of no Supreme Court case *restricting* the *Erie R. R.* v. *Tompkins* doctrine to diversity cases or *excluding* it from the bankruptcy courts generally, as does the opinion below. The *Tompkins* case discussed three classifications of cases in which federal courts should follow state law. The first and second relate to diversity (304 U. S. at pp. 71 and 74) but the third is much broader:

> "*Third. Except* in matters governed by the Federal Constitution or by acts of Congress, the law to be applied in *any case* is the *law of the state.* And whether the law of the state shall be declared by *its Legislature* in a statute or by its highest court in a decision is not a matter of federal concern. There is no federal general common law." (Our emphasis).
>
> **Erie R. R. Co. v. Tompkins (1938) 304 U. S. 64, 78.**

While the great majority of cases invoking the *Tompkins* doctrine are diversity cases, and expression are common in opinions to the effect that the *Tompkins* doctrine applies *in* diversity cases, we know of no case where the Supreme Court has *excluded* its application in other types of cases falling within the purpose of the doctrine. On the contrary, a recent and seemingly competent annotation in **21 ALR2d 256-257** states that the Supreme Court left open the question of whether the *Tompkins* doctrine applies where federal jurisdiction is not based on diversity

in *D'Oench, Duhme & Co.* v. *Federal Deposit Ins. Corp.* (1942) 315 U. S. 447, 456. The annotation goes on to say that on non-federal questions (and the validity of this first mortgage is non-federal) the lower federal courts have been following state law in cases not based on diversity (pp. 256-257).

In a recent diversity case involving a Mississippi statute construed by the state courts almost identically with the Indiana courts' construction of our statute, the Supreme Court applied the *Tompkins* doctrine to require the federal district court to follow the statute as barring an action to recover upon a real estate contract made by a foreign corporation in the unauthorized transaction of business in the state. **Woods v. Interstate Realty Co. (1949) 337 U. S. 535, 536, 538.** The decision below reaches the incongruous and conflicting result that such a contract would be enforced if by fortuitous circumstance or design the debtor or the property were thrown into the forum of a bankruptcy court and the obligation were asserted in the form of a claim instead of a complaint. This conflicting result arises in this case primarily from the failure of the courts below to recognize the basic principles above discussed under (1) and (2) and secondarily from their arbitrary exclusion of the *Tompkins* doctrine from the bankruptcy courts generally.

Certiorari needs to be granted for the purpose of preventing this Court of Appeals' decision from standing as a precedent restricting the Erie R. R. v. Tompkins doctrine to diversity cases and excluding it from the bankruptcy courts generally, and to keep that question open, even though this Court may find that this case turns upon the earlier and more basic doctrines above discussed under (1) and (2) and that it is unnecessary for

it to decide the application of the *Tompkins* doctrine here.

(4)

The Court of Appeals' openly expressed disregard of the Indiana statute, and the expressed disregard of the question of how the Indiana courts would decide the validity of this first mortgage lien (Tr. 126), shows that certiorari is needed to vindicate the statute and the state decisions construing it and to compel the bankruptcy court to follow the state decisions whatever they may be. See quotation from the Court of Appeals' opinion at page 5 of this petition, *supra*.

Moreover, this type of statute is very common in most states, as stated in the Court of Appeals' opinion (Tr. 125) just preceding the passage defying it. This type of statute represents a highly important exercise of the state's police and regulatory power and it widely affects business transactions and the public welfare.

Another of the many dangerous errors in this decision is to turn the bankruptcy courts into a sanctuary where non-complying foreign corporations or their successors in interest can enforce their invalid contracts and reap the fruits of their unauthorized transaction of business in defiance of the state and its courts. (Tr. 126).

Accordingly, it seems unnecessary to demonstrate the Indiana law at length. As indicated in the Court of Appeals' opinion (Tr. 124-125) the statute in effect at the time both of these mortgages were made, penalized a foreign corporation with a fine up to $10,000.00 for doing business in the state without becoming licensed and provided:

> "* * * and, *in addition* to such penalty, if, after this act shall take effect, any foreign corporation

shall fail to comply herewith, *no suit may be maintained, either at law or in equity,* upon *any* claim, legal or equitable, whether *arising out* of contract or tort, in any court in this state." (Our italics)

Section 4918, Burn's Ind. Stats. 1926

(Now substantially re-enacted as Section 18-2328 Burns Ind. Stats. 1933)

The Indiana courts hold under this statute that *if* the non-complying corporation becomes licensed *after* transacting the unauthorized business and after making the unauthorized contract thereon, the contract then *becomes* enforcible in the state courts. The only two Indiana cases cited in the opinions below (Tr. 99, 125) are of this type. *Selph* v. *Illinois Pipe Line Co.* (1934) 206 Ind. 490, 493 and *Peter & Burghard Stone Co.* v. *Carper* (1930) 96 Ind. App. 554, at bottom of p. 599. The latter case contains a dictum that such a contract would be "enforcible by suit in the federal courts" (p. 572) which apparently misled the bankruptcy court in this case (Tr. 99) but that dictum was in 1930 prior to the decision in *Erie R. R.* v. *Tompkins,* 304 U. S. 64 in 1938, and was predicated upon *David Lupton Sons Co.* v. *Automobile Club* (1912) 225 U. S. 489, which was repudiated in the above cited case of *Woods* v. *Interstate Realty Co.* (1949) 337 U. S. 535, 536. Little discussion is needed here concerning the two earlier decisions of the Court of Appeals cited in its present opinion (Tr. 126) since the construction of this statute must be governed by the Indiana decisions. *Metropolitan Life Insurance Co.* v. *Kane,* 117 F. 2d 398, turned principally upon a question of holder in due course (a question not in this record) and was predicated mainly upon the now-repudiated decision in *David Lupton's Sons Co.* v. *Automobile Club* (1912) 225 U. S. 489, *supra.*

The crucial fact in this case which determines the applicable Indiana law is the fact that this non-complying corporate mortgagee, Home Bank & Trust Company, never did comply and **never can comply** because it went out of existence in 1935, four years before bankruptcy jurisdiction attached in 1939, as admitted by respondent Evans in the bankruptcy court (Tr. 48) and expressly found by the bankruptcy court (Tr. 97). This controlling fact (omitted and disregarded in the Court of Appeals' opinion) brings into operation the following *later* Indiana cases construing this statute and holding that where the foreign corporation "had not qualified and could not qualify in Indiana, that was an effective answer in bar" against any recovery on the transaction or contract in an Indiana court:

Barnett v. Central Republic Bank and Trust Co. (1935) 100 Ind. App. 495, 500, 196 N.E. 369, 371.

Burroughs v. Southern Colonization Co. (1932) 96 Ind. App. 93, 103-104, 106, 173 N.E. 716, 719.

The above *Barnett* case involved a fact situation very similar to the one here, where the foreign corporation went out of existence without ever having complied and its individual successor mortgagee-trustee intervened and sought to enforce the mortgage (100 Ind. App. at p. 496) but nevertheless the court held that the original corporate mortgagee's non-compliance and permanent inability to comply created a "proper plea in bar" against enforcement of the mortgage (p. 500). The *Burroughs* case distinguished *Peter & Burchard Stone Co.* v. *Carper,* (1930) 96 Ind. App. 554, 599, *supra,* and held that where the foreign corporation " had not qualified and could not qualify in Indiana on account of its having been put into

the hands of a receiver" this created a good defense in bar against the obligation. (96 Ind. App. at p. 104).

Wherefore, petitioner prays that a writ of certiorari may issue to review the decision below.

JAY E. DARLINGTON,
Attorney for Petitioner.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1952.

No. 467

IN THE MATTER OF V-I-D, INC., DEBTOR.
KELLEY, GLOVER & VALE, INCORPORATED, TRUSTEE,
Petitioner,

vs.

CHARLES J. KRAMER AND HELEN E. KRAMER AND
PETER EVANS, SUCCESSOR INDENTURE TRUSTEE,
Respondents.

BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI.

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RESPONDENTS' BRIEF.

ADDITIONAL STATEMENT OF FACTS.

Respondents, by way of correction of petitioner's statement of facts, and additional thereto, say: In an attempt to confuse the issues Attorney Darlington introduced in evidence, over respondents' objection, a quit claim deed from Glover & Glover to Kelley, Glover and Vale, Incorporated, Trustee, to the real estate involved (Tr. 77). The United States Court of Appeals held heretofore in a prior appeal in this case that said Glovers had no interest in the real estate (158 F. 2d 964), and this Court denied certiorari, 331 U. S. 829 (1947). See also 177 F. 2d 234 (1949), cert. denied 339 U. S. 904 (1950).

The record (Tr. 93) shows respondent Peter L. Evans was named as Successor Trustee under the mortgage indenture, and the District Court authorized and directed him to act and take part in these reorganization proceedings. This order is still in force and binding upon petitioner (Tr. 93).

The first mortgage indenture itself provides for the securing of the indebtedness and bonds (Tr. 80). It further provides that in case of failure to pay any bond when due, at the option of the legal holder, or holders, of said bond, or any of them, the whole issue may be declared due and payable at once and the legal holder, or holders, of said bond, or any of them, or the trustees for the benefit of the legal holders, have the right to foreclose the trust deed (Tr. 83). It also provides (Tr. 85):

> "Each and every estate, right, title, interest, lien, claim, demand and cause of action expressed or intended by this indenture to be vested in or conveyed to the trustees shall (whether or not the same shall be lawfully conveyed to or vested in the Home Bank and Trust Company and its successors in trust hereunder) in any event hereby vest in and be conveyed to Lawrence H. Prybylski and his successors in trust hereunder, and each and every covenant or obligation expressed or intended by this indenture to run in favor of, and each and every right, power, remedy and duty expressed or intended by this indenture to be conferred upon or be enforcible by the Trustee shall (*whether or not the same shall lawfully run in favor of or be conferred upon or be enforcible by the Home Bank and Trust Company or its successors in trust hereunder*) in any event run in favor of, be conferred upon and enforcible by Lawrence H. Prybylski and his successors in trust hereunder with like effect, in each and every such case, as though this indenture were originally entered into between the party of the first part and the said *Lawrence H. Prybylski, as sole Trustee.*"

The Home Bank and Trust Company never acted in its individual capacity, but only as an inactive trustee; and the situs of this loan was Chicago, Illinois (Tr. 51, 52, 53). The bonds were sold in Chicago where they were legal, and the loan was paid out in Chicago (Tr. 54-55). The Home Bank and Trust Company is not before this Court, either individually or as Trustee. It is not claiming anything, but negotiated the loan solely as a broker, and the record shows it owned no bonds. The First Mortgage bonds were bearer bonds and negotiable commercial paper, and sold for value before maturity to third parties, in due course, from whom respondents Charles J. Kramer and Helen E. Kramer purchased the bonds they hold (Tr. 23, 55, 76). The first mortgage and bonds were not dead as stated by the petitioners.

The Home Bank and Trust Company was not the mortgagee, as alleged by petitioner, but merely co-trustee in the mortgage.

The judgment of foreclosure upon which petitioner seeks to rely was on a second mortgage which specifically provided that said mortgage was subject to and junior to the respondents' first mortgage (Tr. 9).

CONTESTED ISSUES.

The District Court and the Court of Appeals both decided the issues that respondents had a good and valid first lien on the real estate according to the facts and law pertaining thereto, and any other decisions would have been contrary to law. Such decisions did not conflict with any other decisions of the United States District Court, the United States Court of Appeals, or the United States Supreme Court, but both decisions followed the Indiana law, and all Federal laws and court decisions, and there is no conflict therein whatsoever.

PROPOSITIONS OF LAW.

I.

A. Respondents' rights are clearly enforceable under Indiana law. First, the trust indenture itself cures any defect which might have been caused by the Home Bank and Trust Company acting as co-trustee. Second, neither original trustee is now before the court, so that the question of their capacity to sue is not presented here. Respondent Evans was authorized and directed by the District Court, on an order not here appealed from, to take part in this reorganization case as present first mortgage indenture trustee to represent bondholders against whom no charge of wrongdoing is being or could be made. Respondents Kramers are specifically authorized under the indenture to sue in their own behalf as bondholders.

Peters, etc. v. *Carper,* 172 N. E. 319 (Ind. App. 1930).

Humphreys v. *City National Bank,* 190 Ind. 293, 130 N. E. 273 (1921).

B. The case of *Woods* v. *Interstate Realty Co.,* 337 U. S. 535 (1949), is inapplicable here because this is not a diversity case. Even if that decision did apply it would result in this Court's following Indiana law, which has already been shown above to support respondents' position. All the cases cited by petitioner support respondents' contentions.

Prudence Realization Corp. v. *Geist,* 316 U. S. 89, 95 (1942).

Vanston, etc. v. *Greene,* 329 U. S. 156.

II.

The Indiana Statute concerning foreign trustees has been held unconstitutional under facts such as shown in this case before the Court.

Kist, et al. v. *Coughlin, et al.*, 50 N. E. 2d 939 (Ind. App. 1943), transferred 57 N. E. 2d 199 (Ind. 1944).

Johnson v. *State, et al.*, 8 N. E. 2d 590 (Ind. 1937).

Robey v. *Smith, et al.*, 30 N. E. 1093 (Ind. 1892).

III.

The cases of *Barnett* v. *Central Republic Bank and Trust Co.* and *Burroughs* v. *Southern Colonization Co. etc.*, cited by petitioner, are not in point, for in those cases the non-qualifying corporations or their successors in interest were creditors suing in their own interest. In the case at bar the respondent bondholders, are the creditors, innocent purchasers of commercial paper for value, and therefore are not chargeable with infirmities. They have the right to foreclose under the specific terms of the bonds and mortgage.

IV.

The Supreme Court will not take on certiorari cases fully heard and adjudicated below for the mere purpose of examining the result.

Deputy v. *duPont*, 308 U. S. 488, 60 S. Ct. 363 (dissenting opinion of Mr. Justice Roberts).

Magnum Import Co. v. *Houbigant, Inc.*, 262 U. S. 159, 43 S. Ct. 531.

ARGUMENT.

I.

Petitioner's contention that the trust indenture is invalid and unenforcible is not supported by Indiana Statutes, by State or Federal court decisions, or by common sense. The indenture vested all the trustee's rights and powers so as to "run in favor of, be conferred upon and be enforcible by Lawrence H. Prybylski and his successors in trust hereunder with like effect, in each and every such case, as though this indenture were originally entered into between the party of the first part and the said Lawrence H. Prybylski as sole Trustee" (Tr. 85). Thus the Statute relied on by petitioner, since it applies only to suits by foreign corporations, is wholly without force in this case.

The Home Bank and Trust Company had no interest whatever in the property individually. This was not an active trust, and the Home Bank and Trust Company does not own any of these bonds; neither does any assignee or successor thereof. All of the cases indicate and hold that the bonds are valid and enforcible without any infirmities. That being so the question of whether the said Bank was doing business in Indiana has no bearing, standing or consideration in determining the matters before the Court.

The Home Bank and Trust Company and Prybylski, former co-trustees for the bondholders, are no longer in existence, and are not before the Court. They are not claiming anything. The bondholders who have bonds that are valid, are proceeding under their mortgage, as the mortgage provides, to collect their indebtedness through enforcement of the trust deed which gives them the right to sue without any action by the named trustees

As for *Woods* v. *Interstate Realty Company*, 337 U. S. 535 (1949), relied on so heavily by petitioner, it should first be emphasized that its doctrine is applicable solely to diversity cases. Throughout the opinion it was made clear that it was for purposes of diversity jurisdiction that the Federal court is "in effect, only another court of the State". *Erie* v. *Tompkins* and its progeny are not controlling where the Federal court, as here, is a bankruptcy court. *Prudence Realization Corp.* v. *Geist*, 316 U. S. 89, 95 (1942).

But even more significant is the fact that all the *Woods* case would require, even if applicable, would be for the court to apply Indiana law, which permits a foreclosure of the first mortgage in the Indiana state courts.

> *Peter and Burghard Stone Co.* v. *Carper*, 96 Ind. App. 554 (Ind. App. 1930).

Thus both the *Woods* case and the *Peter* case, and all other cases cited by petitioner militate against the petitioner's claim in this case, and sustain the contention of the respondents that the bonds are valid, that the indenture is valid, and that the bondholders could sue in either the state courts or the federal courts.

II.

It is the law that no action will fail or fall because of an invalid trustee, or no trustee, for the court can, and upon request by interested parties usually does, appoint a trustee. Burns' Ind. Statutes (1951), Sec. 56-619. Nowhere in the law do you find a cause of action held invalid and unenforcible because of a non-resident trustee where the party beneficially interested has done no wrong and the debt is not invalid for some legal reason.

Petitioner further asserts that two of the trustees named were officers of the bank. That fact can have no bearing on

this case. None of the trustees, including the bank, ever claimed anything under the bearer bonds, or anything under the trust deed, other than as co-trustees, who were wholly inactive titleholders.

III.

The decisions of the District Court and the Court of Appeals are supported by all the evidence in the case, and by the applicable law; and any other decision would have been contrary to both the evidence and the law. The holders and owners of the bonds are authorized by the trust deed to foreclose in their own names, and as the Home Bank and Trust Company, and Prybylski, as trustees, are not involved here, there is no legal reason why the bondholders cannot proceed to collect their just claims. Nor is Peter Evans in any way precluded from maintaining the validity of the bonds as Successor Trustee for bondholders other than the Kramers.

IV.

The Supreme Court will not take, on certiorari, cases fully heard and adjudicated below for the mere purpose of examining the result.

Petitioner, in its brief, fails to set forth any reasons for the granting of the writ sought, other than a dissatisfaction with the manner in which the District Court and Court of Appeals determined the question below, and complaint as to certain language used in the opinion by the Court of Appeals.

This Court will exercise its power of certiorari sparingly and with caution and issue its writ only in matters of great public interest. Its position was well stated by Mr. Chief Justice Taft in *Magnum Import Company* v. *Houbigant, Inc.*, 262 U. S. 159; 67 Law Ed. 922, 43 Sup. Ct. 531:

"The question how the Court should exercise this

power (to issue writ of certiorari) next arises. The jurisdiction to bring up cases by certiorari from the Circuit Court of Appeals was given for two purposes: First, to secure uniformity of decision between those courts in the nine circuits; and second, to bring up cases involving questions of importance which it is in the public interest to have decided by this court of last resort. The jurisdiction was not conferred upon this court merely to give the defeated party in the Circuit Court of Appeals another hearing."

And further, as said by Mr. Justice Roberts in *Deputy* v. *duPont*, 308 U. S. 488, 84 L. Ed. 416, 60 S. Ct. 363:

> "The function of this court is to resolve conflicts of decision and to settle important principles of law. The discretionary power of this court to review judgments of lower Federal Courts was not intended to be exercised in every case where these courts had adjudicated the conflicting claims of the parties, which involves no important principle of law and no conflict of decision amongst the Federal Courts. * * * we will not take cases fully heard and adjudicated below for the mere purpose of re-examining the correctness of the result."

CONCLUSION.

It is therefore respectfully submitted that this case is not a proper one for review by certiorari in this Court, and that the petition for a writ of certiorari should be denied.

Respectfully submitted,

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13

IN THE

Supreme Court of the United States

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IN THE MATTER OF V-I-D, INC.,

Debtor,

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vs.

CHARLES J. KRAMER and HELEN KRAMER, and PETER EVANS, Successor Indenture Trustee,

Respondents.

REPLY BRIEF OF PETITIONER.

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REPLY BRIEF OF PETITIONER.

I.

Respondents' Brief impliedly confesses the basic error of both courts below, of expressly flouting the Indiana statute and decisions. (Tr. 126, 198 F. 2d at p. 395).

This confession takes the form of devoting their entire brief to arguing that the first mortgage claimants could have recovered under Indiana law, plus their statement that petitioner's quarrel is with "certain language" of the opinion. (Br. 8).

Our primary grievance is not with the "language" of the opinion, or even the unjust "result" to petitioner (though the injustice is great). The important ground for certiorari is the **dangerous and dictatorial ground and doctrine** of the decision below, as a precedent. This is shown by the following decisions which the respondents cite against themselves. (Br. 8-9):

> "The function of this court is to *resolve conflicts* of decision and to *settle important principles of law.*" (Our italics).
>
> *Deputy* v. *duPont,* 308 U.S. 488, 84 L. Ed. 416, 60 S. Ct. 363.

> "The jurisdiction to bring up cases by certiorari from the Circuit Court of Appeals was given for two purposes: First, to secure *uniformity* of decision between those courts in the nine circuits; and second, to bring up cases involving *questions of importance* which it is in the *public interest* to have decided by this court of last resort."
>
> *Magnum Import Company* v. *Houbigant, Inc.,* 262 U.S. 159; 67 Law Ed. 922, 43 Sup. Ct. 531.

II.

The question whether respondents **could** enforce the first mortgage and bonds against this real estate in the state courts of Indiana under Indiana law is not the important question now, and need not be determined in ruling upon this petition, either: (1) because this Court will not decide questions which should have been but were not determined below, or (2) because such questions will be deferred until this Court decides the case on the merits.

But if the merits were now before this Court, respondents' statements of law and fact are entirely erroneous and misleading because:

A.

This was a Business Loan of the Bank's Money.

Contrary to respondents' statement that Home Bank and Trust Company was an "inactive trustee" and the "situs of this loan was in Chicago, Illinois" (Br. 3), the District Court made its opinion its finding of facts (Tr. 101) and expressly found in its opinion:

> "The evidence was to the effect that the Home Bank and Trust Company, an Illinois Corporation, was *never licensed* to do business in Indiana; that Lawrence H. Prybylski was a *vice-president* of the bank; that the *bank* made a number of *loans* on Indiana property similar to the (here involved) *Baran* loan; and that *it ceased to exist* as a bank institution about 1935. Some of the mortgages were executed in Indiana and others in Chicago. The Baran mortgage was *executed in Gary, Indiana.* It was the practice of the bank that *after* the trust indentures were signed and recorded and the mortgage bonds were registered at the bank, the *loans* were paid out in Chicago and the bank proceeded to sell the bonds. Under these circumstances, it is concluded that the Home Bank and Trust Company *was doing business in Indiana* at the time of the *execution of the trust indenture.*" (Our italics.) (Tr. 97, 98.)

As indicated in the above finding of the District Court, this mortgage was one of "a number of loans on Indiana property" made by this bank in *carrying on its investment banking business in Indiana.* Respondent Evans so testified (Tr. 49-51) and so did Baran's attorney, Malcjewski, who said this bank made this loan in *competition* with a similar bank in Indianapolis, Indiana (Tr. 62).

Respondent Evans also testified it was the *bank's money* which went to Baran on this loan: "We would pay to the man who *borrowed,* give him the money" (Tr. 54).

The fact that the bank *afterwards* sold these mortgage bonds to undisclosed purchasers at undisclosed times *does not give the bondholders any better lien on the real estate than the bank had* (except a holder in due course as discussed, *infra*). *An assignee or transferee of a non-complying foreign corporation which could not have enforced its claim in the state, is in no better position than the corporation.* To hold otherwise would judicially sanction and encourage evasion of important state laws designed to control foreign corporations:

> **20 C.J.S. Corporations, Sec. 1843, p. 66 at note 90.**
>
> **Standard v. Cantwell (Tex. C.A. 1926), 286 S. W. 760, 7620763 (applying rule to assignee of mortgage notes).**
>
> **Association Collectors Inc. v. Hardman (1940) 2 Wash. 2d 414, 98 P. 2d 318, 319.**

No rights of holders in due course are here involved. Neither opinion below raises the point. The record is devoid of any evidence that respondent Evans, as the bank's successor indenture trustee, presently represents any bondholder who purchased before maturity (1934), or who any such bondholders are or the amount of their holdings. The only identified bondholders are Kramer and wife, holders of $101,000.00 principal amount of the $135,000.00 bond issue (Tr. 124), all of which they purchased as bartering speculators at cut rates after the 1934 maturity date. The District Court's memorandum opinion finds:

> "The evidence was also to the effect that, beginning about 1936, the claimants Kramer and Kramer purchased bonds issued *under* the Baran mortgage, many of the bonds being acquired in exchange for *merchandise*. Some of the bonds were purchased for as low

as 15% of their face value and some as high as 35% of their face value." (Tr. 98.)

A person not a holder in due course is a *mere assignee* who takes the bonds subject to all defenses which might have been made against them in the hands of the original holder, the bank.

Sec. 19,-402, Clause 2, Burns Ind. Stats. 1933.
Baum v. Nord (1928) 88 Ind. App. 674, 680, par. 2, 164 N.E. 294, 296, par. 2.

All claims of the bondholders against this real estate are necessarily *derived* from the bank and *its transaction* in making this loan. This appears on the face of the bonds themselves as set forth in Kramer's claim (Tr. 3) and by the fact that the first mortgage indenture gives either the bank or the bondholders the right to "foreclose *this* trust deed" upon default (Tr. 83). Respondents' argument on this point simply emphasizes that the bondholders' claim against the real estate is *derived through* the bank's mortgage and *the bank's transaction.*

B.

Individual Trustees were Bank Officers.

The bank's original co-trustee, Prybylski, was the bank's vice-president, as recited in the above finding of the District Court and that was "the only reason he was named in these trust indentures" according to Evans' testimony (Tr. 56, top).

Evans was named in the original trust indenture mortgage as the bank's successor trustee "with identical powers and authority" (Tr. 85) because he was the bank's president (Tr. 47). The District Court *substituted* him as trustee under the mortgage during the hearing on the